



STATE OF HAWAII
DEPARTMENT OF ACCOUNTING
AND GENERAL SERVICES

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MAR 8 1990

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COMPTROLLER'S MEMORANDUM NO. 1990-4

TO: Heads of Departments and Agencies
FROM: Russel S. Nagata, Comptroller
SUBJECT: Determining Employer-Employee Relationship

There are 2 purposes for issuing this memorandum, which is our third one on the above subject. The 2 purposes of this memorandum are:

- (1) To modify the "retirement" coding illustrated in a sample of a Form 5 included with one of our earlier memorandums; and
- (2) To require a break in service of at least one day at the end of a three-month period in your contracts with individuals working in an employer-employee relationship.

For background, you may wish to refer to our earlier memorandums on the above subject, which were:

Comptroller's Memorandum No. 1989-7, dated February 22, 1989

Comptroller's Memorandum No. 1989-22, dated December 6, 1989

Retirement Coding on Form 5

In Comptroller's Memorandum No. 1989-22, there was included a sample of a Form 5 which illustrated the "retirement" coding as follows:

"Group" block: N

"FICA" block: N

As confirmed with the Employees' Retirement System, the code in the "FICA" block should be "E", signifying that the individuals working under contract in an employer-employee relationship must be deducted Medicare tax. Although such individuals are not subject to full FICA tax, because they are not eligible for membership in the Retirement System, they are subject to the hospital insurance (Medicare) portion of FICA. The "retirement" coding on the Form 5 sample in Comptroller's Memorandum No. 1989-22 therefore should have been as follows:

"Group" block: N

"FICA" block: E

Break in Service

On the basis of further related discussion with the Employees' Retirement System, there should be at least a one-day break in service at the end of a three-month period when an individual's services are retained under contract, when it has been determined that the services are being performed in an employer-employee relationship for employment tax purposes, and when the individual is therefore being paid through the payroll system so that employment taxes can be deducted and remitted to the appropriate tax jurisdiction.

This requirement for a break in service will help to keep clear that the individual working under contract is not eligible for Retirement System membership or for full FICA coverage through the State. The requirement should also be consistent with contract provisions that the individual does not receive any vacation, sick leave, medical, social security, or retirement benefits.

The break in service as explained in this memorandum should be reflected in the Forms 5 prepared by your agency according to Comptroller's Memorandum No. 1989-22.

Please forward this memorandum to the office in your department or agency which prepares payrolls and, if needed, to personnel offices that may be involved in processing Forms 5 for individuals whose services are retained under contract. Retroactive adjustments must be processed for any Medicare deductions that have been missed, and Forms 5 may need to be amended to reflect the requirement for a break in service. It is therefore important that impacted staff receive this information as soon as possible so that necessary adjustments can be made and all contracts and other related documentation conformed to these instructions.



RUSSEL E. NAGATA
Comptroller